



UNIVERSITI PUTRA MALAYSIA

**CONTROL PATTERNS AMONG
MULTINATIONAL SUBSIDIARIES IN MALAYSIA**

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GSM 2003 11

**CONTROL PATTERNS AMONG
MULTINATIONAL SUBSIDIARIES IN MALAYSIA**

By

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**Thesis Submitted to the Graduate School of Management, Universiti Putra
Malaysia, in Partial Fulfillment of the Requirements for the Degree of
Master of Science**

August 2003



**This thesis is specially dedicated to my family and friends who have stood by me
till the end. May God bless all of you.**

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in partial fulfillment of the requirements for the degree of Master of Science

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August 2003

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Malaysia is currently one of the competitive recipients of foreign direct investments in the Asian region. The stable political and economic environment of the country have attracted foreign multinational corporations (MNCs) to choose and set up business here in Malaysia, hence contributing to her economic growth and development.

This research presents the findings of a survey on foreign subsidiaries in Malaysia, regarding their foreign parents' control patterns over them. Control patterns in this study are divided into two types of control. Behavioral control is mainly the direct control imposed by the foreign headquarters and is measured by the number of expatriates representing the foreign parent in key positions of the local subsidiary. On the other hand, output control reflects indirect or "hands-off" approach of headquarters and is gauged by the frequency of reports submitted to foreign headquarters annually.

This research analyses how these control patterns are associated with the nationality of the foreign parent organization, as well as the level of ownership of foreign parent in a

Malaysian subsidiary. Control patterns are also linked to a third variable, which is the typology of MNCs that is employed by a foreign parent organization.

After receiving feedback from 113 MNCs in Malaysia, the findings support that Japanese MNCs do practice more behavioral control than their European or American counterparts. However, the hypothesis that American MNCs practice more output control than their Japanese or European counterparts is not supported.

As for the level of ownership, one out of two hypotheses is accepted. The analysis indicates that the level of ownership of foreign parent in the Malaysian subsidiary and the use of behavioral control are dependent. On the other hand, the analysis did not discover enough evidence to support that there is a difference in the usage of output control among wholly, majority or minority owned subsidiaries.

Typology of MNCs in this study is divided into two broad categories: global and non-global. Findings indicate that behavioral control and typology of MNCs are dependent. However, the study failed to find significant evidence that points to a difference of output control usage between the two types of MNCs.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi sebahagian keperluan untuk ijazah Master Sains

**POLA KAWALAN DI ANTARA SUBSIDIARI-SUBSIDIARI
MULTINASIONAL DI MALAYSIA**

Oleh

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Malaysia pada masa kini ialah salah sebuah negara saingan utama penerima pelaburan asing terus di rantau Asia. Keadaan politik dan ekonomi yang stabil di negara ini telah menyumbang kepada tarikan syarikat multinasional asing untuk memilih dan memulakan perniagaan di Malaysia, yang seterusnya menyumbangkan kepada pertumbuhan ekonomi dan pembangunan Malaysia.

Tesis ini memaparkan pemerhatian-pemerhatian daripada soal selidik terhadap subsidiari-subsidiari asing di Malaysia berkenaan pola kawalan ibupejabat asing terhadap mereka sebagai subsidiari di Malaysia. Pola kawalan di dalam kajian ini dibahagikan kepada dua jenis kawalan. Kawalan kelakuan ialah kawalan secara langsung yang dibuat oleh ibupejabat asing dan diukur menggunakan bilangan pekerja luar negara yang mewakili ibupejabat asing di dalam jawatan-jawatan utama subsidiari tempatan tersebut. Sebaliknya, kawalan pengeluaran mencerminkan kaedah “lepas tangan” atau secara tidak langsung ibupejabat dan diukur menggunakan kekerapan laporan yang diserahkan kepada ibupejabat asing dalam setahun.

Tesis ini mengkaji bagaimana pola-pola kawalan ini berkait dengan kewarganegaraan organisasi ibupejabat asing, dan juga tahap pemilikan ibupejabat asing di dalam subsidiari Malaysia. Pola kawalan juga dikaitkan dengan pembolehubah ketiga, iaitu jenis organisasi yang digunakan oleh organisasi ibupejabat asing.

Setelah menerima maklumbalas daripada 113 subsidiari multinasional di Malaysia, analisis data menyokong bahawa syarikat multinasional Jepun memang mengamalkan lebih kawalan kelakuan daripada syarikat-syarikat Eropah dan Amerika. Walaubagaimanapun, hipotesis kedua yang menyatakan bahawa syarikat multinasional Amerika mengamalkan lebih kawalan pengeluaran daripada syarikat Jepun dan Eropah tidak disokong.

Mengenai tahap pemilikan pula, satu daripada dua hipotesis telah disokong. Analisis telah membuktikan bahawa tahap pemilikan ibupejabat asing di dalam subsidiari Malaysia dan penggunaan kawalan kelakuan adalah saling bergantung. Sebaliknya, analisis tidak mendapati bukti kukuh untuk menyokong bahawa terdapatnya perbezaan di dalam penggunaan kawalan pengeluaran di antara pemilikan subsidiari secara penuh, majoriti atau minoriti.

Jenis syarikat multinasional di dalam tesis ini dibahagikan kepada dua kategori luas: global dan bukan-global. Pemerhatian menyatakan bahawa terdapat bukti yang cukup untuk menyatakan bahawa kawalan kelakuan dan jenis syarikat multinasional adalah saling bergantung. Namun begitu, kajian ini gagal untuk mencari bukti kukuh bagi menyatakan terdapatnya perbezaan di dalam penggunaan kawalan pengeluaran di antara kedua-dua jenis syarikat multinasional.

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I certify that an Examination Committee met on 30th June 2003 to conduct the final examination of **Raja Nerina bt. Raja Yusof** on her **Master of Science** thesis entitled “**Control Patterns Among Multinational Subsidiaries in Malaysia**” in accordance with Universiti Pertanian Malaysia (Higher Degree) Act 1980 and Universiti Pertanian Malaysia (Higher Degree) Regulations 1981. The committee recommends that the candidate be awarded the relevant degree. Members of the Examination Committee are as follows:

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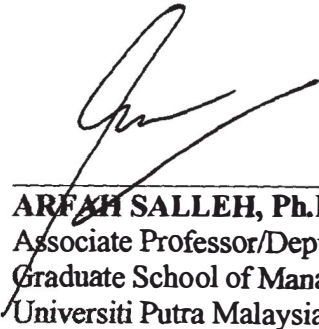
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DECLARATION

I hereby declare that the thesis is based on my original work except for quotations and citations which have been duly acknowledged. I also declare that it has not been previously or concurrently submitted for any other degree at UPM or other institutions.

R Nerina

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Date: *29/8/03*

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LIST OF ABBREVIATIONS

1.	AFTA	Asean Free Trade Area
2.	ANOVA	Analysis of Variance
3.	ASEAN	Association of South East Asian Nations
4.	CFA	Confirmatory Factor Analysis
5.	FDI	Foreign Direct Investment
6.	GFI	Goodness of Fit Index
7.	LISREL	Linear Structural Relations
8.	MIDA	Malaysian Industrial Development Authority
9.	MITI	Ministry of International Trade and Industry
10.	MNCs	Multinational Corporations
11.	MNEs	Multinational Enterprises
12.	RMSEA	Root Mean Square Error of Approximation
13.	SPSS	Statistical Package for the Social Sciences

CHAPTER ONE

INTRODUCTION

Malaysia is one of the developing countries in the Asian region. Malaysia, which was previously an agricultural-based country, slowly turned herself into a manufacturing/industry-based country. The last years of the 20th century witnessed the rapid development of industries in Malaysia that is still continuing until now, despite the setback that occurred during the 1997-1999 Asian economic crisis.

Malaysia continues to be one of the main attractions for foreign direct investments from various countries around the world, attracting approximately 74 percent of its total investments in 2001 (New Straits Times, Feb 6 2002). The stable political and economic conditions, as well as the growing technological facilities and skills in Malaysia, are the main attractions that brought American, European, Japanese and other investors into the country. These multinational corporations, or better known as MNCs, invest in various sectors in the country including manufacturing, agriculture, finance, general services and trading.

When its subsidiary is operating in a different environment, located far from its home office, a foreign parent finds it harder to guide and monitor its subsidiary's performance compared to its domestic operations. However, those are also the main reasons why the home office should keep tight control of its subsidiary for the purpose of achieving results that are consistent with its global strategies and objectives.

Hence, it comes as no surprise that international management control has been and will continue to be one of the important issues faced by multinational corporations. Different multinational corporations from different countries would use different types and degree of control that suit their objectives and complement their cultural behavior.

This research presents the findings of a survey on foreign subsidiaries in Malaysia, regarding their foreign parents' control patterns over them. Basically, this research studies how the control patterns are associated with the nationality of the foreign parent organization, as well as the level of ownership of a foreign parent in a Malaysian subsidiary. Control patterns are also linked to a third variable, which is the type of organizational structure (e.g. global, multidomestic, international etc.) that a foreign organization employs to monitor overseas subsidiaries.

Surprisingly, there are not many local studies regarding control patterns of multinational corporations in Malaysia that have been conducted. One local study was done by Hamdan, June and Raja Azimah in 1992, investigating output control, behavioral control and autonomy.

Other similar studies are from other countries such as the United States, the United Kingdom and Australia, some dating back to the 70's and 80's. These studies proved to be useful guidance in conducting a study here in Malaysia, although careful considerations have been given in adapting their methodology and results to this study.

Background

Even though foreign direct investment activities have long been established on the Malaysian soil, little research has been done to know about business strategies of multinational corporations. The fact that most of the multinational corporations that have invested here come from the developed and developing countries indicates that the onus is on Malaysia to emulate their successful international business management strategies. Since Malaysia herself is not short of budding local multinational corporations, the experience of foreign MNCs here can be a vital and useful guidance for these local MNCs in their international business ventures.

This study incorporates and combines many different aspects of international business management, mainly organizational structure, international control management, organizational behavior, strategic management as well as cross- cultural management.

The basic theme of this study is control. Control, in the international management context, can take on many definitions. However, this study concentrates on control that is defined as “the measures or behavior that the parent firms (in the home country) impose on their subsidiaries (in the host countries) in order to ensure performance of operations and personnel adheres to plans of home office” (Phatak, 1989). Thus, it seems appropriate for such a study to be conducted in Malaysia since she is one of the rapidly developing countries in the Asian region with a growing number of foreign MNCs setting up subsidiaries in the country.

Various studies have tried to relate control patterns to many other characteristics of multinational corporations such as nationality of firms (Hamdan, June and Raja Azimah, 1992; Egelhoff, 1984), size of subsidiaries (Cray, 1984) and types of strategy chosen (Baliga and Jaeger, 1984).

However, this research concentrates on the relationship of managerial control patterns with the level of parent ownership in the Malaysian subsidiaries and typology (organizational model) of MNCs. In addition, the question of whether there is tendency for different nationality of parent firms to favor different types of control is also investigated.

Control and nationality have received much attention because of the differences of culture in different countries. These cultures, in turn, have an effect or impact towards the way different countries manage their businesses abroad. Their style of management might have been passed through many generations; however, in the present world, situations might have changed, hence this study intends to update the previous findings.

In addition, this study also incorporates level of ownership as the second variable to be studied in relation to control. Level or degree of ownership can be regarded as a controlling factor for a parent over its subsidiary (Hamdan, June and Raja Azimah, 1992). This study intends to investigate its association with two different types of controls that is proposed by Ouchi (1977) and Phatak (1989).

Typology of multinational corporations is also included due to its significant role in the structure and strategy of MNCs. Structure and strategy have been, on occasions, related to control (Child, 1972; Ouchi, 1977). Hence, this study, which uses the popular Bartlett and Ghoshal's MNC typology, intends to discover whether different types of MNCs use different control mechanisms or use a particular control type more than the other.

Before proceeding to the core issues of the study, let us take a look at the realm of international business and multinational corporations, and discover their background, roots and roles in the world of global business we know today.

International Business

The term 'international business' itself presents a broad area of study, hence it does not come as a surprise that many different terminologies exist for the term.

According to Asheghian and Ebrahimi (1990), international business is "those business transactions among individuals, firms or other entities (both private and public) that occur across national boundaries".

On the other hand, Ball and McCulloch Jr. (1993) define it as "business whose activities involve the crossing of national borders". To Phatak (1997), international business involves the "business activities of private or public enterprises that involve the movement across national boundaries of resources, goods, services, knowledge or skills".

Phatak (1997) outlines the different forms of international business activity. These forms include:

- Exporting
- Countertrade
- Contract manufacturing
- Licensing
- Franchising
- Turnkey projects
- Equity-based ventures: wholly-owned/joint ventures

History Of International Business

The activity of international business dates back to the ancient times, when the Greeks, Mesopotamian and Phoenician merchants were involved in the import and export of goods and services (Asheghian and Ebrahimi, 1990).

However, international business developed more extensively during the colonial days in the 16th century. At the time, American, Dutch and British colonial traders formed trading firms and established foreign branches throughout Asia (Ball and McCulloch Jr., 1993).

However, well before the arrival of these western colonial powers, Malacca, which is located at a strait of peninsular Malaysia (now known as the Malacca straits), was already a popular port and a bustling center of international business activities,

involving mostly Arabian and Indian traders during the 15th century. This indicated that Malaysia was already a seasoned player in the field of international business and had acted as a host country long before its formation and independence.

Multinational Corporations (MNCs)

A multinational corporation is the principal actor in international business (Asheghian and Ebrahimi, 1990).

Multinational corporations are frequently referred to as MNCs, and are also sometimes cited as multinational enterprises or MNEs. Since both take on the same meaning and are used prevalently in various literature, this study uses both the terms interchangeably.

The term multinational corporation has been conferred different, but not contrasting, definitions. However, one of the widely accepted ones is given by Dunning (1993). He defines an MNE as “an enterprise that engages in foreign direct investment (FDI) and owns or controls value-adding activities in more than one country”. In other words, it is crucial for a corporation to own and operate production or distribution facilities in two or more countries to be characterized as an MNC (Atkinson and Miller, 1998).